

A CALIFORNIA INVESTMENT POLICY FOR THE 21ST CENTURY

Speech by State Treasurer Phil Angelides
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Today I would like to speak with you about the economic challenges we face as Californians – especially since the tragic events of September 11th – and how we must respond in these uncertain times. I want to outline an investment policy that will see us through this difficult period and that will help us to achieve sustainable economic growth in the decades ahead.

I want to begin by providing a little perspective. The decade of the '90s was extraordinary. We had the good fortune to experience a remarkable economic boom that made California the very crucible of the new global economy. California became the wealthiest State in the richest nation on earth.

Then, as is inevitable, the up-cycle ended and a down-cycle began. This year we already were struggling with an economic downturn when some of the most jarring events in our nation's history accelerated the slide. We have been reminded – with the collapse of the dot-com industry, the roiling of the stock market, the emergence of the energy crisis, and the trauma of September 11th – that nothing lasts forever and that, like most things in life, economic progress is continually earned.

And now, everyone is asking: How long will this new turmoil last and how deeply will it affect the economy?

Before I go any further, I just want to say that I am an optimist. I don't believe in foolish optimism, but I do believe that what looks doubtful today can be turned into a solid gain tomorrow.

A story about Harry Truman comes to mind. During his whistle-stop campaign for the presidency in 1948 – in which he proved the pundits wrong and won the election – he refused to be pessimistic despite the heavy odds against him. One day he was speaking from the back of the train, and he asked a man in the crowd how he intended to vote. The man said, "Mr. Truman, I wouldn't vote for you if yours was the only name on the ballot." Truman turned to an aide and said, "Put that man down as doubtful."

I believe we should show the same spirit of determination. As we struggle to survive these difficult times, we should not cast our eyes to the ground despondently. Rather, we should look ahead at the challenges our State will face and, in both the public and private sectors, we must find ways to invest in our physical and human infrastructure to support the enormous growth we will experience in decades to come.

There is no doubt that, in the coming year, the State budget will face tough times. With the economy slowing and tax revenues declining, we face a projected budget deficit of \$8 billion to \$14 billion. So we must do what any family would do in tough times – cut back on spending. Yet, even as they watch their pennies, prudent families make an effort to plan ahead – setting aside money for their children’s education, or even looking to buy their first home when prices are down and interest rates are low.

Similarly, as the Governor and the Legislature struggle to close the budget shortfall, we must take advantage of the resources at our disposal – from our pension and investment funds to our ability to issue bonds at historically low interest rates – that can serve as the engines of our financial recovery and build our long-term economic strength.

If you will indulge me in a personal example, when I was running my own real estate investment and management business during the recession of the early ‘90s, I spent much of my time trimming the costs of our projects that were struggling so I would have the resources to invest in the new ventures that would build my company’s future.

In the business world, the smart investors excel during hard times. In every recession, they look for new opportunities and deploy their capital wisely to fund the ventures which will grow as the economy rebounds. This requires sound money management, toughness, dedication, and faith in the future.

Franklin D. Roosevelt, who presided over our nation in the dark days of the Great Depression and World War II, said, “The only limit to our realization of tomorrow will be our doubts of today.”

California’s rise to economic preeminence after World War II is a testament to the power of vision and the willingness to invest in the future. A previous generation of leaders – from Earl Warren to Goodwin Knight to Pat Brown – had the courage to look ahead and make investments in the public infrastructure that still sustain us – nearly half a century later. They gave us a world renowned water project that gave life to dry fields and distant cities. They gave us a nine-campus university system and a 23-campus state university system that educated the best workforce in the world. And they gave us a transportation system that, in its heyday, was unequaled.

Now is the time to revive the legacy of those leaders. We are a State of wealth, capacity, and potential. We must find ways to use our assets to reinvigorate our economy today and create wealth for future generations of Californians. Even in this time of budget stress, we are not without resources. Here are a couple of examples.

The State of California’s \$300 billion pension and investment portfolio represents the largest pool of capital in the global marketplace. Now is the time to focus this capital on California, to invest in badly needed infrastructure and economic development projects which will stimulate growth in this critical time period and for decades to come.

With long-term tax exempt interest rates at the lowest levels since 1969, the State has an extraordinary opportunity to finance, over a 30-year timeframe, public investments of value to today's economy and of critical importance to our future economic strength. Our State has the capacity to issue upwards of \$25 billion in bonds over the next four years, with transaction structures which minimize payments in the upcoming budget years. Now is the time to move forward with the financing and construction of critical public needs – such as school repair and construction – that constitute the public fabric of any successful economy. Now is the time to finance the water supply, conservation and environmental protection projects that will meet our State's needs for the decades to come. And now is the time to accelerate the funding of public investments in areas such as information technology which can improve our productivity and give ballast to critical sectors of our economy.

Felix Rohatyn – the highly respected investment expert who served as U.S. Ambassador to France, and who led New York City out of bankruptcy in the 1970s – wrote something in the *Wall Street Journal* on September 25th that I want to quote. He wrote:

A large-scale public investment program would have an important long-term economic impact and is badly needed by urban as well as rural America. It would also provide a great psychological lift to Americans worried about the future.

Mr. Rohatyn is correct. This is the right investment policy for these times, and it is consistent with what the Treasurer's Office has advocated since I took office – even when the economy was more robust. Investing in our future is good business and necessary whether we are in troubled economic waters or enjoying smooth sailing in the seas of prosperity.

In June of 1999, my office issued a report called *Smart Investments* in which we articulated the need for a State public investment policy to keep California strong into the 21st Century.

In May of 2000, we built on our *Smart Investments* initiative by launching a new policy effort – *The Double Bottom Line: Investing in California's Emerging Markets*. That initiative called on the public and private sectors – from public pension funds to venture capitalists – to invest in California's communities in a way that achieves the “double bottom line” objectives of strong returns and broadened economic opportunity in our State.

In those two reports, we outlined a set of investment policies and programs to respond to the challenges which California will face in the years ahead. And we noted that of all the challenges before us, there are two in particular which will threaten our sustained economic progress in coming decades if we do not respond adequately.

The first challenge is to find a way to meet the tremendous demands of projected growth, while preserving those unique environmental qualities that have been so much a part of California's economic strength.

Over the next 20 years, California will add 12 million new residents, more than 5 million new jobs, and 4 million new households. Two million children will be added to our public school system. Even more startling is the fact that this growth will exceed that seen during the boom years of the 1950s, 1960s and 1970s combined!

We need to embrace a set of policies – including investment initiatives – to change the growth patterns we have experienced for decades because they threaten to degrade the environment and make California a less attractive place to live and work.

We must commit ourselves to curbing sprawl and to reinvigorating the communities within our existing urban fabric. Our public policies – from water supply and conservation to transportation to open space preservation – must foster a new era of environmentally sustainable growth for the 21st Century.

The second overarching challenge that we noted in *Smart Investments* and *The Double Bottom Line* – and one that is even more daunting – is to find ways to grow that promote equality of opportunity across our State. For future economic strength will be elusive if there are “two Californias” – with much of the State enjoying prosperity while at the same time there are communities suffering from economic decline and devastation.

These two challenges are still squarely in front of us, even as we enter a period of recession. California will continue to experience growth over the long term – meaning we must remain committed to making the investments in our public fabric that will sustain us in the years ahead. We made the mistake in the early '90s of failing to focus on our growth challenges and have been paying the price in areas like water, energy, and transportation ever since. And, the recession is likely to exacerbate the economic opportunity gap which has persisted despite the boom of the '90s.

Since we launched our *Smart Investments* and *Double Bottom Line* efforts, we have been hard at work putting in place public investment programs and initiatives to respond to our long-term economic challenges. We intend to redouble our efforts as we enter this period of economic uncertainty.

Here are some examples of what the Treasurer's Office has done over the past three years to direct public expenditures in a way that builds our communities today and for the future.

- At the Tax Credit Allocation Committee, which I chair, we adopted new criteria for awarding federal and State tax credits for the construction and rehabilitation of affordable rental housing. We now give priority to projects in struggling neighborhoods in which the housing is part of a comprehensive revitalization effort. We also reward projects which meet a set of sustainable

development goals – for example, projects within walking distance of transit, schools, parks, and shopping. And, as importantly, we successfully fought, over the past year, to increase annual funding for this critical program from \$450 million to \$650 million.

- At the California Infrastructure and Economic Development Bank, we have launched a new low-cost loan program for local infrastructure projects. This precious resource will be targeted to economically distressed communities, in support of projects which are environmentally sensible.
- I successfully pushed for adoption of the Extra Credit Teacher Home Purchase Program – a \$164 million initiative which will provide down payment assistance, low interest mortgages, and tax credits to assist teachers, willing to serve in low performing schools, in purchasing a home. The program aims to bolster schools in poor neighborhoods and to recruit and retain teachers with experience and capability.
- Since January of 1999, we have provided financing for nearly \$700 million in water supply, conservation, and environmental protection projects to meet the needs of a growing population and economy. And at the Infrastructure Bank, we are now launching a new leveraged financing program with the capacity to issue up to \$2 billion in bonds – dramatically increasing State lending for the construction of wastewater and water recycling facilities, and other conservation programs.
- And, from January 1999 through today, we have financed over \$5.5 billion in public school construction and repair to meet the needs of a growing population and economy.

Of course, we recognize that public works and community development programs are only one tool in a wide array of State public policy initiatives that must be pursued to meet the challenges of sustainable growth and economic opportunity. That is why we also have diligently labored to mobilize the powerful instrument of financial capital in ways that bolster California's future economic prospects.

In this regard, we have put in place a set of investments which begin to fulfill the promise of our *Double Bottom Line* and *Smart Investments* initiatives.

Here is some of what we have done:

- The Treasurer's Office has purchased \$960 million in home mortgages made under the Community Reinvestment Act to low and moderate income families and communities, providing new capital to lenders to make even more loans.
- We have increased State deposits in California lending institutions by \$2.9 billion, making available well-priced capital for home and business lending.

We are now depositing State funds with over 120 community lenders in our State, serving a broad range of urban and rural markets.

- CalPERS and CalSTRS, in the last year, have committed over \$1.5 billion in new capital investment for real estate development – from mixed use to office to commercial to housing – targeted to California communities. \$400 million has been allocated for affordable housing, a critical need for our residents and our economy.
- CalPERS has just launched the California Initiative – a \$475 million venture fund to grow businesses in underserved neighborhoods.
- And, at my urging, CalPERS and CalSTRS each have adopted a goal of investing 2 percent of their portfolios – that totals about \$5 billion – in California’s underserved communities – our own emerging markets.

To summarize, we have been able to make a fundamental shift in State investment policies and to direct more than \$12 billion in State resources and investment capital over a three-year period into pursuit of the policies we outlined in the *Smart Investments* and *Double Bottom Line* initiatives.

I cite these initiatives, not to pat myself on the back, but to give you an idea of the ways that California can use its vast resources to boost our economy today and to create enduring economic strength in the years ahead. We have the means to ensure that California has sustainable growth. As important, we can also ensure that the gap between the “two Californias” – which was wide during prosperous years – does not become a gaping chasm in lean years. This is not a new idea.

After the nation had made slow but steady progress against the Depression, it plunged into a recession in the summer of 1937. President Franklin D. Roosevelt responded in the spring of 1938 with an investment program to assist economic recovery. I want to quote from his Fireside Chat radio address to the American people on April 14, 1938.

In the first century of our republic we were short of capital, short of workers and short of industrial production, but we were rich, very rich in free land, and free timber and free mineral wealth. The federal government of those days rightly assumed the duty of promoting business and relieving depression by giving subsidies of land and other resources.

Thus, from our earliest days we have had a tradition of substantial government help to our system of private enterprise. But today the government no longer has vast tracts of rich land to give away and we have discovered, too, that we must spend large sums of money to conserve our land from further erosion and our forests from further depletion. The situation is also very different from the old days because now we have

plenty of capital, banks and insurance companies loaded with idle money; plenty of industrial productive capacity and many millions of workers looking for jobs. It is following tradition as well as necessity, if government strives to put idle money and idle men and women to work, to increase our public wealth and to build up the health and strength of the people – to help our system of private enterprise to function again.

I submit that we may well find ourselves today in a similar situation. And this makes it all the more imperative that, as we reduce State spending to balance our budget on the one hand, we look at the investment tools that are still available to rebuild our infrastructure and our economy for the decades of growth that lie ahead.

Despite our current challenges, I believe we are on the verge of a great era in California – if we approach it wisely. We can sustain the California Dream in the 21st Century if we summon the strength in this time of crisis to invest anew in our economy and our people.

Thank you for the opportunity to speak to you today, and to describe an investment policy that will prepare us for a bright future.